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INFO RUCNCLS/ALL SOUTH AND CENTRAL ASIA COLLECTIVE  
RUCPDO/DEPT OF COMMERCE WASHDC  
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RUEATRS/DEPT OF TREASURY WASHDC  
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RHMFIUU/FAA NATIONAL HQ WASHINGTON DC  
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UNCLAS SECTION 01 OF 02 NEW DELHI 002554

SIPDIS  
SENSITIVE

STATE FOR SCA/INS AND EEB  
USDOC FOR ITA/MAC/OSA/LDROKER/ASTERN/KRUDD  
DEPT PASS TO USTR CLILINFELD/AADLER/CHINCKLEY  
DEPT PASS TO TREASURY FOR OFFICE OF SOUTH ASIA MNUGENT  
TREASURY PASS TO FRB SAN FRANCISCO/TERESA CURRAN

E.O. 12958: N/A

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SUBJECT: MOBILE BANKING PROMISES FINANCIAL INCLUSION BUT REGULATIONS  
HOLDING IT BACK

REF: MUMBAI 555

1. (SBU) Summary. Two means to financial inclusion in India -- business correspondents and mobile banking -- have been slow to take hold, hampered by rules from India's cautious central bank (see reftel). Though the central bank allowed the business correspondents model -- where intermediaries offer on-site banking opportunities in unbanked rural and urban areas -- in early 2007, Econoffs found no signs that it had gained traction. Similarly, though some in the government expressed excitement with the promise of mobile banking, regulators have yet to finalize rules in this area and the growth of mobile banking is therefore on hold for now. The spread of mobile bankingservices will largely depend on RBI willingness to loosen know-your-customer regulations that impose heavy administrative costs on small account holders. End summary.

Business Correspondents -  
Bridge to Isolated Communities  
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2. (U) Business correspondents (BCs) were first endorsed by a Reserve Bank of India (RBI) internal group on Rural Credit and Micro-Finance (the "Khan Committee") headed by Shri H.R. Khan, Chief General Manager and Principal at the RBI's College of Agricultural Banking in a report issued July 19, 2005. BCs were subsequently allowed by the RBI in a January 2006 circular as a financial inclusion effort to spread access to banking services to the unbanked, mainly India's poor. BCs perform basic banking transactions in rural or urban slum communities that lack access to brick-and-mortar bank branches.

3. (SBU) RBI regulations allow only certain people to act as BCs, though the list of those allowed - teachers, ex-service members, ex banking officials, etc. - is broad and was expanded in April 2008. Pulla Rao, Banking Supervision General Manager at the RBI in New Delhi, told Econoffs that BCs do not need to be certified or licensed by regulators, but they do need to be approved by a bank that can be audited and disciplined if it is found to be in violation of the RBI guidelines.

4. (SBU) However, even as the new regulations enlarged the scope of eligible BCs, the RBI also added a new restriction that limited BCs to 15 kilometers from a base branch in rural areas and 5 kilometers from a base branch in urban areas. When asked about the controversial regulations, RBI's Rao stated that the regulations were presently under review. [Comment: A Business Standard article in May pointed out that there are 600,000 villages in India, but only 45,000 rural bank branches, suggesting that the 15 kilometer limit would severely limit the potential reach of BCs. End comment.]

5. (SBU) Responses from officials at both private and public banks regarding their use of BCs tended to indicate that BCs are not gaining traction within their institutions. Rajnish Datta, president of Small Business Banking at Yes Bank in New Delhi, had not even heard of the concept, and other banking officials did not evidence much enthusiasm. Officials at state-owned Punjab National Bank (PNB), for instance, said that they did have a BC program, but that it was in phase one of a pilot. They could not provide specificity as to how many BCs the pilot program was using, saying

only that it was "a number" of them. Likewise, Rao could not provide a good estimate of the degree to which BCs are being used nationally because the RBI does not collect data on BC usage.

16. (SBU) Shashank Saxena, a new Director of Banking at the Ministry of Finance, expressed skepticism about the BC model, saying that the costs of BCs were too high. He said that despite there being no brick-and-mortar cost to BCs, administering small accounts was nevertheless costly. He suggested that financial inclusion was instead best facilitated through an interest rate subsidy financed through a financial inclusion fund. [Note: Two such funds already exist - the Financial Inclusion Fund for developmental and promotional activities, and the Financial Inclusion Technology Fund to meet the costs of technology adoption for those services. End note.]

Mobile Banking

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17. (U) Mobile banking falls into two`QQQo55), whereas MDB uses specialized electronic banking devices that are used by personnel affiliated with a bank.

18. (SBU) Private sector interlocutors tended to be enthusiastic about MPB, though primarily because of the potential it presents to broaden access to banking services with an estimated 200 million mobile phone subscribers in India. Ministry of Finance's Saxena voiced more skepticism and caution, saying that while mobile phones reached 200 million people in India, they were the richest 200 million and if the goal is to reach the poor, it wouldn't be done through MPB. [Note: Bharti Airtel, a leading telecom provider, has indicated that half of new subscriptions are from rural residents. Total subscriptions in India now top 300 million. End note.] Rao acknowledged that MPB had good potential to reach into rural areas. The RBI's main concern, however, is with know-your-customer (KYC) rules which ensure that money transfer is performed non-anonymously to prevent criminal activity.

19. (SBU) Officials at the Ministry of Finance and the RBI were generally enthusiastic about MDB, saying that pilots of MDB had performed well. The RBI is in the process of issuing regulations on mobile banking, and draft regulations are currently out for public comment. Rao said that for the near term at least, mobile banking would only be allowed for informational purposes - checking the balance of bank accounts for instance - but not for transactional purposes like making deposits or transferring funds.

110. (SBU) Econoffs asked Rao about a mobile banking pilot program in Delhi - a joint project between mobile phone company EKO and HDFC bank - in which mobile phone users are automatically given a bank account with the same number as their mobile phone. The advantage of this is that mobile phone users can establish a bank account without having to verify their address, a task that can be difficult for the poor. Rao said that HDFC had notified them of the project and that the RBI is allowing the program to continue because there are only a couple hundred users and their transactions are small.

Comment

11. (SBU) A significant obstacle to financial inclusion is the necessity of KYC rules. There is a tradeoff between having strong KYC practices and getting people into the banking system. Terrorists, criminals, and the poor share the characteristic of being undocumented -- the former intentionally so, the latter by the nature of poverty -- making distinguishing between the two a labor- and time-intensive process of physical visits to places of residence and interviews of friends and neighbors. The cost of this relative to potential revenue from the poor's meager savings has kept traditional banking to the poor unprofitable. New technologies and practices, like BCs and MPB can change the cost calculus, if regulators and the banking system can get behind them.

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